



1984

## Torts - Commercial

Lyman G. Hughes

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### Recommended Citation

Lyman G. Hughes, *Torts - Commercial*, 38 Sw L.J. 35 (1984)  
<https://scholar.smu.edu/smulr/vol38/iss1/3>

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# TORTS—COMMERCIAL

by  
Lyman G. Hughes\*

## I. COMPETITIVE PRACTICES

### A. Antitrust

CERTAINLY the most significant development in the area of competitive torts during the survey period was the enactment by the legislature of the Texas Free Enterprise and Antitrust Act of 1983 (TFEAA).<sup>1</sup> The TFEAA represents a wholesale revision of the Texas antitrust laws, which have remained relatively unchanged since 1903. A detailed examination of the TFEAA is beyond the scope of this survey article, but an overview may be helpful to the practitioner who may have had occasional contact with the former state antitrust statutes and who will undoubtedly have far more contact with the TFEAA.

Generally, the prescriptive provisions of the TFEAA are found in the first four subsections of section 15.05, which parallel sections 1 and 2 of the Sherman Act<sup>2</sup> and sections 3 and 7 of the Clayton Act.<sup>3</sup> These sections prohibit combinations in restraint of trade, monopolization and attempted monopolization, exclusive dealing arrangements, and certain acquisitions and mergers.<sup>4</sup> The TFEAA expressly states that, with one important exception discussed below,<sup>5</sup> the act shall be construed in harmony with federal judicial interpretations of comparable federal antitrust statutes.<sup>6</sup> Given this directive, the Texas courts should abandon the confusing and inconsistent assortment of cases decided under the prior statutes and begin anew with decisions that follow federal precedents.

The TFEAA allows the state to bring civil suits for civil penalties, which may range up to one million dollars for a corporation,<sup>7</sup> and for injunctive

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\* B.A., Kansas State University; J.D., Southern Methodist University. Attorney at Law, Carrington, Coleman, Sloman & Blumenthal, Dallas, Texas.

1. Texas Free Enterprise and Antitrust Act, ch. 519, §§ 1-3, 1983 Tex. Gen. Laws 3010 (codified at TEX. BUS. & COM. CODE ANN. §§ 15.01-.26 (Vernon Supp. 1984)) [hereinafter cited as TFEAA].

2. 15 U.S.C. §§ 1-2 (1982).

3. *Id.* §§ 14, 18.

4. TFEAA § 15.05(a)-(d). The TFEAA also contains provisions relating to the right to work and labor union activities. *Id.* § 15.05(e)-(f).

5. The TFEAA will only be construed in harmony with constructions of federal statutes to the extent such constructions are consistent with the objectives of the Act. *Id.* § 15.04; *see infra* notes 25-28 and accompanying text.

6. TFEAA § 15.04.

7. *Id.* § 15.20(a).

relief.<sup>8</sup> In the case of an unlawful merger or acquisition the court may order divestiture in a government action upon a finding that "no other remedy will eliminate the lessening of competition."<sup>9</sup> Criminal sanctions are also available under the Act.<sup>10</sup>

Private rights of action<sup>11</sup> are available to any person or governmental entity "whose business or property has been injured by reason of any conduct declared unlawful in Subsection (a), (b), or (c) of Section 15.05 of this Act."<sup>12</sup> Under the state antitrust statutes prior to the TFEAA only actual damages could be recovered.<sup>13</sup> Consequently, violations of the prior state antitrust laws were most commonly asserted either as pendent claims in federal antitrust actions in federal courts or defensively in suits to collect debts arising from courses of dealing that allegedly violated the antitrust laws.<sup>14</sup> The TFEAA changes prior law by allowing treble damages in private suits when the trier of fact finds the unlawful conduct "willful or flagrant."<sup>15</sup> The availability of such damages will certainly increase both offensive use of the state antitrust provisions and the number of antitrust actions brought in the state courts. Plaintiffs should bear in mind, however, that any action found by the court to be groundless and brought in bad faith, or for the purpose of harassment, may result in an award of attorneys' fees, court costs, and other expenses to the defendant.<sup>16</sup>

The practitioner will probably encounter the TFEAA in the form of civil investigative demands issued by the Texas attorney general's office.<sup>17</sup> Broadly stated, the TFEAA allows the attorney general to utilize all of the discovery tools available in civil litigation, prior to the institution of a lawsuit, in order to collect information or documentary material that is "relevant to a civil antitrust investigation."<sup>18</sup> The provisions setting forth the

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8. *Id.* § 15.21(b).

9. *Id.* § 15.20(b).

10. *Id.* § 15.22.

11. Private plaintiffs may seek damages and/or injunctive relief. *Id.* § 15.21(a)-(b).

12. *Id.* § 15.21(a)(1). It is important to note that the quoted language tracks the provisions of § 4 of the Clayton Act, 15 U.S.C. § 15 (1982), with respect to parties who have standing to assert antitrust violations. The legislature apparently intended no private right of action to exist for a violation or a threatened violation of § 15.05(d) relating to mergers and acquisitions. Undoubtedly, however, conduct that would violate § 15.05(d) would also violate § 15.05(a), and a private cause of action could be brought under the latter subsection.

13. Competitive & Trade Practices Act, ch. 785, § 15.32, 1967 Tex. Gen. Laws 2553, 2566-67 (repealed (1983)).

14. *Climatic Air Distribs. v. Climatic Air Sales, Inc.*, 162 Tex. 237, 345 S.W.2d 702 (1961); *Patrizi v. McAninch*, 153 Tex. 389, 269 S.W.2d 343 (1954); *Grand Prize Distrib. Co. v. Gulf Brewing Co.*, 267 S.W.2d 906 (Tex. Civ. App.—San Antonio 1954, writ ref'd n.r.e.).

15. TFEAA § 15.21(a)(1).

16. *Id.* § 15.21(a)(3).

17. *Id.* § 15.10. It is hoped that the attorney general's office will utilize the broad civil investigative demand powers in lieu of filing lawsuits and conducting the investigation through judicial discovery.

18. *Id.* § 15.10(b). Curiously, the legislature did not authorize the issuance of a civil investigative demand to "a proprietorship or partnership whose annual gross income does not exceed \$5 million." *Id.* This exception does not seem well reasoned. No justification exists for a corporation having annual gross income of \$100,000 to be subject to a demand while a partnership in the same line of business with gross annual income of \$1,000,000 is not. More fundamentally, why any person or entity with relevant information or document

procedures governing such demands are complex and not completely consistent with respect to document demands, written interrogatories, and depositions.<sup>19</sup> The practitioner should carefully review the provisions of section 15.10 of the TFEAA when confronted with an investigative demand. A party receiving a demand may protect its rights only by taking timely procedural steps specified in the statute.<sup>20</sup> In addition, counsel should be aware of the availability of broad "transactional" immunity that the TFEAA accords a person exposed to self-incrimination by replying to an investigative demand.<sup>21</sup>

Finally, the TFEAA includes a mechanism for filing a declaratory judgment action by a person<sup>22</sup> who is "uncertain of whether or not his or her action or proposed action violates or will violate the prohibitions contained in Section 15.05 . . . ."<sup>23</sup> The time-consuming nature of such an action, however, together with the severe restrictions the act places upon the use of any declaratory judgment obtained, suggests that this provision of the TFEAA will be utilized rarely, if ever.

The TFEAA undoubtedly represents a vast and long overdue improvement in the antitrust law of this state. Gone are the inflexible and antiquated per se prohibitions of the former statute that often resulted in tortuous court opinions seeking to circumvent the plainly unjust results that would have resulted from a literal reading of the statutes. Gone, too, is the rule that allowed a just debt to go unpaid upon a mere showing that the debt was related to a contract that, albeit unintentionally, violated the state antitrust laws.<sup>24</sup>

The TFEAA is not without its troublesome points, however. Two provisions of the TFEAA stand out as potentially problematic. First and foremost is the last clause of the "purpose" section of the Act.<sup>25</sup> That section provides that the TFEAA will be construed in harmony with federal interpretations of comparable federal statutes but only to the extent that such interpretations are consistent with the objective of the TFEAA to "maintain and promote economic competition . . . and to provide the benefits of

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should be exempt from an investigative demand, as long as the demand is not unreasonably burdensome or oppressive, is not clear.

19. For example, confidential information requested by written interrogatory or contained in requested documents can be designated as containing trade secrets or confidential information and given some protection from disclosure. *Id.* § 15.10(i)(5). The Act provides no comparable means of protecting from disclosure the same information elicited in deposition testimony.

20. *Id.* § 15.10(f).

21. *Id.* § 15.13.

22. The TFEAA excludes from its definition of "persons" who may institute such a declaratory judgment action "a foreign corporation not having a permit or certificate of authority to do business in this state." *Id.* § 15.16(a). This author submits that such an exclusion may be of questionable constitutionality.

23. *Id.* § 15.16(a).

24. *See, e.g.,* Climatic Air Distribs. v. Climatic Air Sales, Inc., 162 Tex. 237, 243, 345 S.W.2d 702, 704 (1961) (manufacturer denied recovery on contract granting exclusive area); Patrizi v. McAninch, 153 Tex. 389, 393-94, 269 S.W.2d 343, 346-47 (1954) (seller unable to recover royalties on contract restricting trade).

25. TFEAA § 15.04.

that competition to consumers in the state."<sup>26</sup> This qualification arguably gives Texas courts the freedom to pick and choose which federal decisions to follow based upon each court's determination of whether the rule of the case benefits consumers. For example, the "direct purchaser" requirement of *Illinois Brick Co. v. Illinois*<sup>27</sup> clearly forecloses consumers from asserting certain claims, such as price fixing at the wholesale level. The language of the TFEAA seems to permit a Texas court, consistent with the stated purpose section of the TFEAA, to ignore *Illinois Brick* and allow indirect consumer-purchasers to pursue an action under the TFEAA.<sup>28</sup> Nevertheless, this author submits that the goal of the TFEAA to bring state law more in line with federal law and to achieve predictability in its application<sup>29</sup> should weigh against discarding federal precedent on the ground that it does not sufficiently benefit consumers.

A second important provision, the interpretation of which will have a major impact on the development of the TFEAA, is the requirement that the unlawful conduct be "willful"<sup>30</sup> or "flagrant"<sup>31</sup> before treble damages are available. If the standard is relatively easy to meet, actions under the TFEAA will proliferate; if the standard is rigorous, however, plaintiffs will probably continue to rely on federal law with its automatic treble damages.<sup>32</sup>

The courts have not yet decided whether the TFEAA should apply retroactively to conduct that occurred before the act became effective;<sup>33</sup> consequently the courts may yet be required to deal with the provisions of the old law. *Mendelovitz v. Adolph Coors Co.*,<sup>34</sup> decided during the survey period, demonstrates the nimbleness that courts have displayed in deciding issues under the previous Texas antitrust statute. The plaintiff in *Mendelovitz*, a beer wholesaler, brought an action alleging that he was cut off from his supply of Coors beer because he sold the beer outside of an assigned territory. The distributor who serviced the plaintiff refused to sell

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26. *Id.*

27. 431 U.S. 720 (1977).

28. By adopting the TFEAA with its federal-like standing requirement in the face of *Illinois Brick*, the legislature arguably intended to accept the indirect purchaser limitation.

29. The mere effort to determine which federal interpretation to apply to the TFEAA should be sufficiently difficult in view of the conflicting federal decisions. The Act contains, of course, no requirement that the Texas courts look to the law of the Fifth Circuit or any other federal circuit. See *supra* note 6 and accompanying text.

30. TFEAA § 15.21(a)(1). "Willful" presumably implies that the defendant intended to violate the law, not that he merely intended to engage in the act found to be unlawful.

31. TFEAA § 15.21(a)(1). The choice of the term "flagrant" by the legislature is curious. The term has no generally recognized legal connotation, and in common parlance it often signifies something open and notorious. The most egregious antitrust violations, on the other hand, are often those that are covert and secret.

32. See 15 U.S.C. § 15 (1982).

33. Under the Texas Code Construction Act, if it applies, the TFEAA would be given prospective application only, and a violation of the antitrust statutes prior to the effective date of the TFEAA would be unaffected by the revision. TEX. REV. CIV. STAT. ANN. art. 5429b-2, §§ 3.02, 3.11 (a) (3) (Vernon Supp. 1984). It may be argued, however, that the TFEAA is not governed by the Code Construction Act. Cf. *Knight v. International Harvester Credit Corp.*, 627 S.W.2d 382, 384 (Tex. 1982).

34. 693 F.2d 570 (5th Cir. 1982).

to him because of the extraterritorial sales, and other distributors refused to sell to him because he was located outside of their territories. The plaintiff asserted both federal and state antitrust claims against Adolf Coors Company and its distributor. He claimed the defendants violated the Sherman Act by imposing territorial restrictions and by combining to boycott him. He based his state law claim on the Texas rule prohibiting a manufacturer from allocating exclusive territories to its distributors.<sup>35</sup> The Fifth Circuit affirmed the trial court's directed verdict in the defendants' favor on the federal claims based upon a "rule of reason" analysis.<sup>36</sup> The court had to deal differently with the state antitrust claims, however, because a "rule of reason" analysis was at least facially unavailable under the old statute.<sup>37</sup> Prior to the TFEAA, granting the exclusive right to sell a product within a given territory was per se illegal under state law.<sup>38</sup> Although the contract in question did not on its face grant an exclusive territory, the plaintiff in *Mendelovitz* claimed that Coors accomplished the same effect by limiting a distributor's sales to a certain territory and appointing only one distributor per territory. The court circumvented the application of the state statute, however, by holding that, even accepting the plaintiff's argument, the exclusive territory restrictions were not the cause in fact of plaintiff's injury.<sup>39</sup> The court reasoned that even with more than one distributor in the plaintiff's area, none of them could have sold to him because of the plaintiff's territorial violations.<sup>40</sup> The court's reasoning is not a model of clarity. The author hopes that the TFEAA will reduce the need for such awkwardness in dealing with Texas antitrust law.

### B. Use of Trade Secrets

In *Zoecon Industries v. American Stockman Tag Co.*<sup>41</sup> the defendants prepared a list of their employer's customers and subsequently used this list to solicit sales for their own company. Ninety-four percent of the new company's sales were to customers on this list. The Fifth Circuit held that the use of a "customer list" of one's former employer violates Texas common law when (1) the former employees are under a duty not to disclose the list, and (2) the list contains information not generally available to the public.<sup>42</sup> The court found the first element of this test easily satisfied in *Zoecon* because the employees had enjoyed a confidential relationship

35. See TEX. BUS. & COM. CODE ANN. § 15.03 (Vernon 1968) (amended 1983).

36. 693 F.2d at 575. The rule of reason analysis requires the trier of fact to weigh all the circumstances of the case in determining whether the restrictive practice is an unreasonable restraint on competition.

37. *Climatic Air Distribs. v. Climatic Air Sales, Inc.*, 162 Tex. 237, 243, 345 S.W.2d 702, 706 (1961); *Anheuser-Busch Brewing Ass'n v. Houck*, 88 Tex. 184, 190, 30 S.W. 869, 870 (1895).

38. *Climatic Air Distribs. v. Climatic Air Sales, Inc.*, 162 Tex. 237, 243, 345 S.W.2d 702, 706 (1961).

39. 693 F.2d at 578.

40. *Id.*

41. 713 F.2d 1174 (5th Cir. 1983).

42. *Id.* at 1179. The court noted that the requirement that the information not be generally available to others in the trade is an element added by Texas law to the traditional

with their former employer and, in addition, had executed employment agreements containing restrictions on the disclosure of confidential information following termination of their employment.<sup>43</sup> The second element was also satisfied, the court concluded, because the customers in the trade involved were not easily identifiable and the list contained information about the particular needs of each customer.<sup>44</sup> The court therefore affirmed the trial court's award of a permanent injunction and exemplary damages.

*Zoecon* illustrates a point of practice worth noting. Under Texas law a trade secret must in fact be secret; in other words, it must not be generally known or ascertainable by others in the same business.<sup>45</sup> Thus, if a person's customers or potential customers could be easily ascertained by those in the trade (as, for example, all restaurants are customers or potential customers of a wholesale food market) a mere list of the customers' names would not be protected. The same list may achieve the status of a trade secret, however, if it contains items of information regarding the customer's or potential customer's business that could be ascertained only from dealing with or attempting to deal with the customer.<sup>46</sup>

### C. *Interference with Prospective Contractual Relationships*

In two cases decided during the survey period the Fifth Circuit addressed the Texas common law tort of interference with prospective contractual relationships. In *Phillips v. Vandygriff*<sup>47</sup> the court merely recited the established Texas law that in order to establish a cause of action a plaintiff must show "that (1) there was a reasonable probability that he would have entered into a contractual relationship; (2) defendant acted maliciously by intentionally preventing the relationship from occurring with the purpose of harming plaintiff; (3) the defendant was not privileged or justified; and (4) actual harm or damage occurred as a result."<sup>48</sup>

The first and second elements of the test recited in *Phillips* were the focus of attention in *Verkin v. Melroy*.<sup>49</sup> *Verkin* involved the tangled web of brokers through whom commercial property often passes before sale. Though the facts were complex, in substance the plaintiff brokers claimed to have been deprived of a prospective contractual relationship that would have yielded a commission on the ultimate sale of the land in issue. The claim arose from the defendant's attempt to bypass the plaintiffs and negotiate directly with the seller, agreeing to pay all commissions in exchange

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definition of a trade secret. *Id.*; see *Gaal v. BASF Wyandotte Corp.*, 533 S.W.2d 152 (Tex. Civ. App.—Houston [14th Dist.], 1976, no writ).

43. 713 F.2d at 1178.

44. *Id.* at 1177.

45. *Mercer v. C.A. Roberts Co.*, 570 F.2d 1232, 1235-39 (5th Cir. 1978).

46. 713 F.2d at 1179-80.

47. 711 F.2d 1217 (5th Cir. 1983).

48. *Id.* at 1230 (quoting *Leonard Duckworth, Inc. v. Michael L. Field & Co.*, 516 F.2d 952, 956 (5th Cir. 1975)).

49. 699 F.2d 729 (5th Cir. 1983).

for a reduction in the purchase price. The trial court granted the defendant's motion for judgment notwithstanding the verdict on the ground that there was no evidence to support the jury's finding of the first two elements of the cause of action. The Fifth Circuit reversed and reinstated the jury verdict.<sup>50</sup>

Of particular interest is the *Verkin* court's discussion of the requirement that "malicious intent" be shown. The trial court had concluded that there was no evidence that the defendant even knew of the plaintiffs and therefore the defendant could not have acted with the intent to block plaintiffs' prospective contractual relationship and to harm the plaintiffs. The appellate court held, however, that the evidence established that the defendant knew that *someone* had a prospective contractual relationship, in the form of a contractual right to a brokerage commission, and that the defendant had acted to cut off that prospective relationship.<sup>51</sup> The defendant did not have to know of the plaintiff's specific identity. Moreover, the evidence showed that the defendant knew that but for his action some other broker would normally receive a commission. The Fifth Circuit held such knowledge sufficient to show intent to harm.<sup>52</sup>

## II. DECEPTIVE TRADE PRACTICES

The issue of who is a consumer under the Texas Deceptive Trade Practices—Consumer Protection Act (DTPA)<sup>53</sup> occupied both the legislature and the courts during the survey period. Of greatest significance is the decision of the Texas Supreme Court in *Flenniken v. Longview Bank & Trust Co.*<sup>54</sup> The plaintiffs in *Flenniken* contracted with Easterwood for the construction of a house. The plaintiffs paid Easterwood \$5010 and executed a \$42,500 mechanic's lien note naming Easterwood as payee. The note was further secured by a deed of trust that named a bank's vice president as trustee. Easterwood assigned the note and lien to the bank in return for the bank's commitment to provide interim construction financing. The bank made advancements, but Easterwood misappropriated the funds and abandoned the construction. The bank foreclosed on the property. The owners' suit challenged the foreclosure as an unconscionable course of action in violation of the DTPA and sought treble damages and attorneys' fees. The trial court found the bank's action unconscionable, and the bank did not challenge the finding on appeal. Instead, the bank contended that the plaintiffs were not consumers under the DTPA.<sup>55</sup> The court of appeals held that the plaintiffs could not sue under the DTPA because, although they were consumers as to Easterwood, they were not consumers as to the

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50. *Id.* at 734.

51. *Id.*

52. *Id.* at 733.

53. TEX. BUS. & COM. CODE ANN. §§ 17.41-.63 (Vernon Supp. 1984).

54. 661 S.W.2d 705 (Tex. 1983).

55. TEX. BUS. & COM. CODE ANN. § 17.45(4) (Vernon Supp. 1984) defines "consumer" as "an individual . . . who seeks or acquires by purchase or lease, any goods or services."



bank.<sup>56</sup> The supreme court reversed.<sup>57</sup>

The court rejected the reasoning of the court of appeals that the foreclosure was not an act that occurred in connection with the purchase of goods or services by the plaintiffs.<sup>58</sup> Instead, the supreme court held that from the plaintiffs' perspective but one transaction took place, the purchase of a house, and the bank's unconscionable act grew out of this transaction.<sup>59</sup> The court held that the plaintiffs, therefore, "were consumers as to all parties who sought to enjoy the benefits of that transaction, including the Bank."<sup>60</sup> The court premised its holding on *Knight v. International Harvester Credit Corp.*,<sup>61</sup> which the court of appeals in *Flenniken* had found distinguishable. Conversely, the supreme court distinguished *Riverside National Bank v. Lewis*,<sup>62</sup> which the court of appeals had found controlling.<sup>63</sup> The supreme court's reasoning seemed sound in distinguishing *Riverside*, but its reliance upon *Knight* was less secure.

While the supreme court was plainly willing to expand the scope of the term "consumer" in the DTPA, the legislature chose to narrow it somewhat in amendments to the DTPA adopted during the survey period. Section 17.45(4) of the DTPA now excludes from the definition of consumer "a business consumer that has assets of \$25 million or more, or that is owned or controlled by a corporation or entity with assets of \$25 million or more."<sup>64</sup> A business consumer is, in turn, "an individual, partnership, or corporation who seeks or acquires by purchase or lease, any goods or services for commercial or business use. The term does not include this state or a subdivision or agency of this state."<sup>65</sup> Apparently the legislature has concluded that a large business is sophisticated enough not to require the protection of the DTPA.<sup>66</sup>

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56. *Longview Bank & Trust Co. v. Flenniken*, 642 S.W.2d 568, 570-71 (Tex. App.—Tyler 1982).

57. 661 S.W.2d at 708.

58. *Id.* at 707.

59. *Id.*

60. *Id.*

61. 627 S.W.2d 382, 388-89 (Tex. 1982) (extension of credit in installment sales contract simultaneously with purchase of vehicle is service contract under DTPA), *cited in Flenniken*, 661 S.W.2d at 706-07. The court of appeals distinguished *Knight* on the ground that *Knight* involved only a single, nonseverable transaction, whereas the court considered the transaction in *Flenniken* to be divisible. The court of appeals thus determined the interim construction financing was not an award of goods or services to the Flennikens by the bank. 642 S.W.2d at 571.

62. 603 S.W.2d 169 (Tex. 1980) (one who seeks only money in transaction is not a consumer), *cited in Flenniken*, 661 S.W.2d at 707-08. The supreme court distinguished *Riverside* on the basis that the Flennikens did not seek to borrow money but to purchase a house. 661 S.W.2d at 708.

63. 642 S.W.2d at 570.

64. TEX. BUS. & COM. CODE ANN. § 17.45(4) (Vernon Supp. 1984).

65. *Id.* § 17.45(10).

66. Section 17.42 was also amended to provide that a business consumer with assets of \$5 million or more according to the most recent financial statement of the business consumer prepared in accordance with generally accepted accounting principles that has knowledge and experience in financial and business matters that enable it to evaluate the merits and

In *Pace v. State*<sup>67</sup> the Texas Supreme Court held that treble damages under the DTPA are not recoverable from the Real Estate Recovery Fund.<sup>68</sup> Because the Fund was established to reimburse persons who suffer "monetary damages" stemming from certain acts of unscrupulous real estate dealers,<sup>69</sup> the court held that treble damages, being in the nature of punitive damages, are not recoverable from the Fund.<sup>70</sup>

Finally, in *Marley v. Drexel Burnham Lambert, Inc.*,<sup>71</sup> the United States District Court for the Northern District of Texas addressed the question of whether, under the Supremacy Clause of the United States Constitution,<sup>72</sup> the federal Arbitration Act<sup>73</sup> preempts the nonwaiver provision of the DTPA<sup>74</sup> with respect to contracts involving interstate commerce. Marley brought an action in regard to an agreement entered into with the defendants for the purchase and sale of commodities futures contracts. Among the claims he asserted was a claim under the DTPA that Marley contended was pendent to a federal claim under the Commodity Exchange Act.<sup>75</sup> The court stayed the action and directed that arbitration be conducted pursuant to an arbitration clause in the contract.<sup>76</sup> The arbitrator dismissed all the plaintiff's claims. Upon a motion by the defendants in the district court to confirm the arbitration award, plaintiff argued that the contractual arbitration clause was ineffective as to the DTPA claims. The court rejected the argument and held that the clearly conflicting provisions of the DTPA and the federal Arbitration Act must be resolved in favor of the federal statute.<sup>77</sup> Thus the DTPA claims were subject to the arbitrator's determination.

The decision in *Marley* was unquestionably correct. The United States Supreme Court recently held in *Southland Corp. v. Keating*,<sup>78</sup> a case rendered subsequent to the *Marley* decision, that a nonwaiver provision in the California Franchise Investment Law<sup>79</sup> similar to that in the DTPA conflicted with section 2 of the federal Arbitration Act and violated the Supremacy Clause.<sup>80</sup> The Court further held that the contractual arbitration clause in issue must be enforced irrespective of whether the issue was

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risks of a transaction and that is not in a significantly disparate bargaining position may by written contract waive the provisions [of the DTPA].

*Id.* § 17.42. The cautious practitioner drafting a contract containing such a waiver would be wise to include recitations and representations by the waiving party that the conditions of § 17.42 are met.

67. 650 S.W.2d 64 (Tex. 1983).

68. TEX. REV. CIV. STAT. ANN. art. 6573a, § 8 (Vernon Supp. 1984).

69. *Id.* § 8(1)(a).

70. 650 S.W.2d at 65.

71. 566 F. Supp. 333 (N.D. Tex. 1983).

72. U.S. CONST. art. VI, cl. 2.

73. 9 U.S.C. §§ 1-14 (1982).

74. TEX. BUS. & COM. CODE ANN. § 17.42 (Vernon Supp. 1984).

75. 7 U.S.C. §§ 1-26 (1982).

76. 566 F. Supp. at 334.

77. *Id.*

78. 104 S. Ct. 852, 79 L. Ed. 2d 1 (1984).

79. CAL. CORP. CODE § 31512 (West 1977).

80. 104 S. Ct. at 858, 79 L. Ed. 2d at 11-12.

raised in state or federal court.<sup>81</sup>

### III. EMPLOYER-EMPLOYEE RELATIONS

Two major developments during the survey period affect an employer's relations with its employees. The most dramatic development came from the legislature in the enactment of the Commission on Human Rights Act.<sup>82</sup> The decision of the Texas Supreme Court in *Otis Engineering Corp. v. Clark*,<sup>83</sup> on the other hand, will have a more subtle and potentially more far-reaching effect.

The scope of this Article does not permit a detailed review of the new Commission on Human Rights Act. Nevertheless, employers and their counsel undoubtedly must become familiar with the Act. The Act does two major things. First, it establishes for the first time in this state a broad statutory prohibition against discrimination in employment on the basis of race, color, handicap, religion, sex, national origin, or age.<sup>84</sup> Second, the Act establishes a state Human Rights Commission<sup>85</sup> and a procedure for administrative review of discrimination complaints.<sup>86</sup> The fundamental purpose of the Act is to create a deferral agency meeting the criteria of federal law<sup>87</sup> and thereby to establish on the state level a mechanism for reviewing discrimination complaints.<sup>88</sup> The Act applies to employers having fifteen or more employees<sup>89</sup> and contains provisions relating specifically to employment agencies<sup>90</sup> and labor organizations.<sup>91</sup> Generalization is, of course, dangerous. Nevertheless, the state act basically conforms to existing federal law in describing prohibited conduct. In some instances the statute specifically addresses issues not clearly resolved under federal law. For example, an employer may, but is not required to, provide health insurance benefits for all abortions.<sup>92</sup> Also, addiction to an illegal or controlled substance and addiction to the use of alcohol are not treated as handicaps.<sup>93</sup> In large part, however, an employer who has been in compliance with federal law will be in compliance with the new Texas Act.

The new Act has brought major changes in the manner in which employment discrimination prohibitions are enforced. The state commission created by the Act, rather than the federal Equal Employment Opportu-

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81. *Id.* at 860-61, 79 L. Ed. 2d at 15.

82. Ch. 7, §§ 1.01-10.05, 1983 Tex. Gen. Laws, 1st Called Sess. 37 (codified at TEX. REV. CIV. STAT. ANN. art. 5221k (Vernon Pam. Supp. 1971-1983)).

83. 27 Tex. Sup. Ct. J. 100 (Nov. 30, 1983).

84. TEX. REV. CIV. STAT. ANN. art. 5221k, §§ 1.01-.04 (Vernon Pam. Supp. 1971-1983).

85. *Id.* § 3.01.

86. *Id.* § 6.01.

87. See Equal Employment Opportunity Act, 42 U.S.C. § 2000e-5(c) (1976).

88. TEX. REV. CIV. STAT. ANN. art. 5221k, § 1.02(1) (Vernon Pam. Supp. 1971-1983).

89. *Id.* § 2.01(5).

90. *Id.* § 5.02.

91. *Id.* § 5.03.

92. *Id.* § 1.04(c). An employer's health insurance plan must, however, provide health insurance benefits for abortion if the life of the mother would be endangered were the fetus carried to term. *Id.*

93. *Id.* § 2.01(7)(B).

nity Commission, will provide the initial administrative review of complaints filed by aggrieved parties.<sup>94</sup> Complaints must be filed within 180 days after the alleged unlawful practice.<sup>95</sup> The commission will determine, after an investigation, whether reasonable cause exists to believe discrimination has occurred.<sup>96</sup> The commission has the authority to bring an enforcement action to effectuate the Act's purposes,<sup>97</sup> and, in addition, complainants may bring private actions after the expiration of time periods similar to those in title VII of the federal Civil Rights Act of 1964.<sup>98</sup> The remedies available under the state act are generally those previously available under federal law.<sup>99</sup>

The Texas Commission on Human Rights Act will certainly be important to every employer, but its impact is generally no broader than the twenty-year-old Civil Rights Act of 1964.<sup>100</sup> The Act will not require employers to alter their practices dramatically. The same cannot be said, however, for the impact of the Texas Supreme Court's decision in *Otis Engineering Corp. v. Clark*.<sup>101</sup> This controversial decision may require employers to make major changes in their manner of dealing with employees.

Otis's employee, Matheson, had a history of drinking while on the job at Otis's, Carrollton, Texas, plant. On the night in question, Matheson appeared intoxicated and in danger of falling into the machine at his work station. His superior suggested that Matheson go home and, according to the majority opinion, escorted him to his car. Three miles from the plant Matheson was involved in an automobile accident that killed two women. The medical examiner found that Matheson had a blood alcohol content of 0.268%, which, to say the least, indicated a highly intoxicated state.<sup>102</sup> In an ensuing wrongful death action by the husbands of the deceased women, the trial court granted summary judgment for Otis on the ground that as a matter of law Otis owed no duty with respect to the off-duty, off-premises tort of its employee. The court of appeals reversed,<sup>103</sup> and the supreme court affirmed.<sup>104</sup>

At issue in the supreme court was the principle that an employer is ordinarily liable for the off-duty torts of his employees only if they are commit-

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94. *Id.* § 6.01(a).

95. *Id.*

96. *Id.* § 6.01(b).

97. *Id.* § 6.01(e).

98. *Id.* § 7.01(a).

99. *Id.* § 7.01(c)-(d).

100. 42 U.S.C. § 2000a (1976).

101. 27 Tex. Sup. Ct. J. 100 (Nov. 30, 1983).

102. The medical examiner testified that the blood alcohol content indicated Matheson had consumed an amount of alcohol representing some 16 to 18 cocktails if consumed over a period of one hour or 20 to 25 cocktails if consumed over a period of two hours. The doctor further testified that 100% of persons with that much alcohol exhibit signs of intoxication observable to the average person.

103. *Clark v. Otis Eng'g Corp.*, 633 S.W.2d 538 (Tex. App.—Texarkana 1982).

104. 27 Tex. Sup. Ct. J. at 103.

ted on the employer's premises or with the employer's chattels.<sup>105</sup> The supreme court concluded, however, that Otis had exercised "control" over Matheson when his supervisor removed him from his employment assignment.<sup>106</sup> This action was sufficient to render Otis liable for Matheson's conduct after he left the plant. The court stated, "What we must decide is if changing social standards and increasing complexities of human relationships in today's society justify imposing a duty upon an employer to act reasonably when he exercises control over his servants."<sup>107</sup> Relying heavily on Prosser<sup>108</sup> and the conclusion that Matheson's supervisor had engaged in an affirmative act by sending Matheson home, the court fashioned a new standard of duty for all pending and future cases:

[W]hen, because of an employer's [sic] incapacity, an employer exercises control over the employee, the employer has a duty to take such action as a reasonably prudent employer under the same or similar circumstances would take to prevent the employee from causing an unreasonable risk of harm to others. Such a duty may be analogized to cases in which a defendant can exercise some measure of reasonable control over a dangerous person when there is a recognizable great danger of harm to third persons. . . . Additionally, we adopt the rule from cases in this Restatement area that the duty of the employer or one who can exercise charge over a dangerous person is not an absolute duty to ensure safety, but requires only reasonable care.<sup>109</sup>

The court therefore remanded the case to the trial court for a determination of the reasonableness of the supervisor's actions.<sup>110</sup> The court listed a number of considerations that should bear upon the determination. The court stated that the trier of fact should be allowed to consider the availability of Otis's nurses' aid station, whether it was possible for the supervisor to telephone Matheson's wife or have another person drive Matheson home, the reasonableness of merely dismissing Matheson early rather than terminating his employment, and the foreseeable consequences of Matheson's driving upon a public street in his stuporous condition.<sup>111</sup>

Four justices dissented in a forceful opinion. The dissent first noted that no court in any jurisdiction had ever held an employer liable for the off-duty, off-premises torts of an intoxicated employee if the employer did not contribute to the employee's intoxication.<sup>112</sup> Next the dissent demonstrated that the precedent cited by the majority wholly failed to support the extension of employer liability adopted by the court.<sup>113</sup> Finally, and perhaps of greatest interest to employers and their counsel, the dissent dis-

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105. RESTATEMENT OF TORTS (SECOND) § 317 (1964); *see* *Pilgrim v. Fortune Drilling Co.*, 653 F.2d 982, 985-86 (5th Cir. 1981) (applying Texas law and following Restatement).

106. 27 Tex. Sup. Ct. J. at 102.

107. *Id.*

108. W. PROSSER, *THE LAW OF TORTS* § 56 (4th ed. 1971).

109. 27 Tex. Sup. Ct. J. at 103 (Nov. 30, 1983).

110. *Id.*

111. *Id.*

112. *Id.* (McGee, J., dissenting).

113. *Id.* at 105-08.

cussed the probable effects of the majority's holding.<sup>114</sup>

Although the dissent may be accused of overstating somewhat the Draconian consequences that may befall employers by reason of the majority's rule, two questions raised by the dissent certainly bear careful consideration. First, it is not clear what action by an employer will constitute exercising control over the employee.<sup>115</sup> The court gave no hint as to how an employer may avoid exercising control over an intoxicated employee short of leaving him at his work station, a danger to himself and to other employees. The facts in *Otis* represented a very minimal degree of control.<sup>116</sup> Indeed, as the dissent noted, the entire basis of the plaintiffs' claim was that Otis *failed* to control its employee. Second, the Otis opinion raises the question of what steps an employer, who by its "affirmative actions" has assumed the duty to prevent its employee from causing an unreasonable risk to others, must take to fulfill that duty. As the dissent noted, the usual practice among employers is to allow an incapacitated employee to leave work.<sup>117</sup> This course of action seems no longer permissible under *Otis*. As the dissent stated, "In an attempt to do justice in this one case, the majority has placed an impractical and unreasonable burden upon *all* employers."<sup>118</sup>

#### IV. FRAUD

Another major development in tort law came from the legislature in the form of amendments to statutory provisions governing fraud in real estate and stock transactions.<sup>119</sup> The amendments were necessary to correct a conceptually troublesome aspect of the statute. Prior to the legislative action, section 27.01 of the Texas Business and Commerce Code clearly required that the plaintiff in a suit concerning real estate or stock fraud prove a requisite mental state to recover against the person making the allegedly false statement<sup>120</sup> or promise.<sup>121</sup> On the other hand, a plaintiff could establish joint and several liability against a person who merely benefited from the false statement or promise irrespective of that person's mental state.<sup>122</sup> Thus in some instances a person who innocently and unknowingly benefited from the wrongful act of another could find himself jointly

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114. *Id.* at 108-09.

115. *See id.* (discussion of uncertainty as to what action constitutes control).

116. Some misunderstanding between the majority and dissent is apparent with respect to the steps the Otis supervisor took at the time of sending Matheson home. The majority stated that the supervisor escorted Matheson to his car and inquired whether he was able to make it home. The dissent stated that the supervisor did no more than release Matheson at the door of the plant. The dissent suggests that if the supervisor's actions were an "affirmative act," then omission, nonfeasance, and inaction are no longer viable concepts in Texas law. *Id.* at 108.

117. *Id.* at 108-09.

118. *Id.* at 109 (emphasis in original).

119. Fraud—Real Estate or Stock Transactions Act, ch. 949, § 1, 1983 Tex. Gen. Laws 5208 (codified at TEX. BUS. & COM. CODE ANN. § 27.01(b)-(e) (Vernon Supp. 1984).

120. TEX. BUS. & COM. CODE ANN. § 27.01(a)(1)(A) (Vernon 1968).

121. *Id.* § 27.01(a)(2)(B).

122. *Id.* § 27.01(b) (amended 1983).

and severally liable for the actions of the true wrongdoer. It is not difficult to imagine a variety of circumstances in which the statute could work an injustice.

One such situation presented itself in *Carr v. Hunt*,<sup>123</sup> a case decided by the Dallas court of civil appeals. Although the facts of the case were complex, the essence of the plaintiff's complaint in *Carr* was that he had been induced to sell a particular tract of land in reliance upon false promises by the buyer. The buyer in turn sold the land to a third party and failed to perform his promises to the plaintiff. The tract of land subsequently became more valuable, and so the plaintiff sought rescission of both sales, relying on the unamended section 27.01. The plaintiff obtained a verdict in the trial court based upon a jury finding that the second buyer knowingly benefited from the first buyer's false promises.

The appellate court held, however, that no evidence supported the finding that the second buyer knew of the false statements or knowingly benefited from the false promises.<sup>124</sup> Nevertheless, the second buyer had plainly benefited, albeit innocently, from the fraud and thus was arguably jointly and severally liable with the party who made the false promises. The court stated that such a result would be anomalous and held that section 27.01(b) would not be read to allow rescission against bona fide purchasers of real estate.<sup>125</sup> The court supported its holding by finding a conflict between the literal reading of section 27.01 and Business and Commerce Code section 24.02,<sup>126</sup> which protects the title of a bona fide purchaser without notice of his seller's fraud.

The legislature amended section 27.01 to correct the inequitable result perceived by the court in *Carr v. Hunt*. Specifically, it amended subsections (b) and (c) of the statute to provide that a person who makes a false statement or false promise is liable for actual damages.<sup>127</sup> Such person is also liable for exemplary damages if he makes the statements "with actual awareness of the falsity thereof."<sup>128</sup> Moreover, the legislature added a new subsection (d), which provides:

A person who (1) has actual awareness of the falsity of a representation or promise made by another person and (2) fails to disclose the falsity of the representation or promise to the person defrauded, and (3) benefits from the false representation or promise commits the fraud described in Subsection (a) of this section and is liable to the

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123. 651 S.W.2d 875 (Tex. App.—Dallas 1983, no writ).

124. *Id.* at 880-81.

125. *Id.* at 881.

126. TEX. BUS. & COM. CODE ANN. § 24.02 (Vernon 1968).

127. *Id.* § 27.01(b)-(c) (Vernon Supp. 1984). The legislature also deleted the measure of damages previously set out in the statute. The statutory measure had been the difference between the value of the real estate or stock as represented or promised and its actual value in the condition in which it was delivered at the time of the contract. *Id.* § 27.01 (Vernon 1968) (amended 1983). Presumably, the courts are now free to fashion whatever measure of damages seems suitable to the circumstances.

128. *Id.* § 27.01(c) (Vernon Supp. 1984). The legislature removed the statutory limitations on exemplary damages to twice the amount of actual damages. Thus the court are now free to grant larger exemplary damage awards.

person defrauded for exemplary damages. Actual awareness may be inferred where objective manifestations indicate that a person acted with actual awareness.<sup>129</sup>

The changes in the statutory fraud section thus eliminate potential liability of a party who acts without knowledge of a prior fraud. On the other hand, a party who benefits from a prior fraud, with knowledge of the fraud, is considered equally culpable with the party who commits the fraud. In this regard the new statute is much more in accord with common sense principles.<sup>130</sup>

## V. LIBEL

In *Golden Bear Distributing Systems v. Chase Revel, Inc.*<sup>131</sup> the Fifth Circuit wrestled with difficult questions of Texas libel law in a case in which the literal statements in the allegedly libelous article were true, but the overall impression they created was false. The defendant published an article describing an investment fraud lawsuit and various legal troubles of a California company named "Golden Bear of California." The plaintiff, a completely separate company known as "Golden Bear of Texas," operated as a franchisee of the California company but had never been accused of any wrongdoing. Nevertheless, the article referred to statements by the Texas company's marketing director, and in describing the alleged fraud of the California company, the article stated that "Golden Bear[s] promises were consistent throughout the country."<sup>132</sup> The jury found the overall impression conveyed by the article was to impute falsely the fraudulent conduct of the California company to the Texas company.

The Fifth Circuit affirmed the trial court judgment for the plaintiff. The court held that the trial court properly submitted to the jury the question of whether the article was defamatory even though it did not literally state that the Texas company had engaged in any wrongdoing. The court stated:

We conclude that the district court correctly followed Texas law in submitting the article to the jury. . . . Since the overall import of the article was capable of two interpretations, one of which was potentially defamatory, it was proper for the trial judge to submit the article to the jury. The jury found the overall effect of the article to be defamatory because the article imputed wrongdoing to Golden Bear of Texas.<sup>133</sup>

The court similarly reasoned that truth was not a defense in this instance. Although the individual statements in the article about Golden Bear of

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129. *Id.* § 27.01(d).

130. The legislature also added a new subsection (e) to § 27.01, providing: "Any person who violates the provisions of this section shall be liable to the person defrauded for reasonable and necessary attorney's fees, expert witness fees, costs for copies of depositions, and costs of court." *Id.* § 27.01(e).

131. 708 F.2d 944 (5th Cir. 1983).

132. *Id.* at 947.

133. *Id.* at 948.



Texas were true, the jury found the overall effect to be defamatory. The court held that for the truth defense to apply, the defamatory interpretation of the article must be true.<sup>134</sup>

Finally, the *Golden Bear* court held that the plaintiff had overcome the possible privilege defense<sup>135</sup> by a showing that the defendant had published the article with reckless disregard for the truth.<sup>136</sup> Critical to affirming the jury's finding of recklessness was the evidence that after the article was published Golden Bear of Texas contacted the defendant, offered to prove it was innocent of any wrongdoing, and asked defendant to print a retraction. The defendant refused to allow the plaintiff to present such proof. The court held, without benefit of Texas authority, that the refusal, together with the defendant's failure to conduct its own investigation to determine if Golden Bear of Texas participated in the investment fraud, supported the jury's finding of recklessness.<sup>137</sup> This author submits that in so holding the court needlessly went too far.<sup>138</sup> A rule that would require publishers to entertain every offer to prove a published statement incorrect at the risk of having the refusal of such an offer later submitted as evidence of recklessness places an unreasonable burden on publishers. Moreover, such a rule seems contrary to Texas law. It is an established principle that a publisher's failure to investigate the truth of a statement before publishing the statement is not evidence of malice.<sup>139</sup> It is illogical to suggest that the failure to investigate the truth of a statement *after* it is published is not subject to the same legal principle. The author's state of mind at the time the statement is published is the critical issue.<sup>140</sup> Only in rare circumstances is the conduct of the defendant after the publication relevant to the question of the publisher's state of mind at the time of publication.<sup>141</sup>

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134. *Id.* at 949.

135. The plaintiff asserted a privilege defense on the basis of TEX. REV. CIV. STAT. ANN. art. 5432 (Vernon 1958). The court held that the defendant failed to carry its burden to show that the article was a "reasonable and fair comment or criticism of . . . matters of public concern published for general information." 708 F.2d at 949 (quoting TEX. REV. CIV. STAT. ANN. art. 5432, § 4 (Vernon 1958)).

136. 708 F.2d at 949.

137. *Id.* at 950. The court relied upon RESTATEMENT OF TORTS (SECOND) § 580A comment d (1976), which states that "[u]nder certain circumstances evidence [of a refusal by a publisher to retract a statement after it has been demonstrated to him to be both false and defamatory] might be relevant in showing recklessness at the time the statement was published." This author suggests that it is more than a small leap from the circumstances described in the *Restatement* to the circumstances present in the instant case, in which the defendant merely declined the plaintiff's offer to attempt to demonstrate that the article was false and defamatory.

138. The court also made statements regarding the showing of malice, but these statements were dicta since the court held that the defendant had not sustained its burden of showing a defense of privilege and the plaintiff was not a public figure. *See* 708 F.2d at 949.

139. *Dun & Bradstreet, Inc. v. O'Neil*, 456 S.W.2d 896, 901 (Tex. 1970).

140. *See Gaines v. Cuna Mut. Ins. Soc'y*, 681 F.2d 982, 989 (5th Cir. 1982); *Foster v. Upchurch*, 624 S.W.2d 564, 566 (Tex. 1981).

141. The only circumstances suggested by the *Restatement* comment relied upon by the court in *Golden Bear* involved conduct by a defendant who has actual knowledge after publication that the statement was both false and defamatory. *See* RESTATEMENT OF TORTS (SECOND) § 580A comment d (1976).

In *Hajek v. Bill Mowbray Motors, Inc.*<sup>142</sup> the supreme court held that the constitutional right of free speech<sup>143</sup> forbids the prior restraint of a defamatory statement.<sup>144</sup> The court therefore dissolved an injunction prohibiting the defendant from driving about the community with the message painted on his vehicle that the plaintiff had sold him a “lemon.”

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142. 647 S.W.2d 253 (Tex. 1983).

143. TEX. CONST. art. I, § 8.

144. 647 S.W.2d at 255.

